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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Memorandum of Ex Parte Presentation

Marlene H. Dortch, Secretary
Federal Communications Commission
-48 12th Street, SW
Washington, DC 20554

Re: CC Docket No. 01-338, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers;
CC Docket No. 96-98, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; and
CC Docket No. 98-147, Deployment of Wireline Services Offering Advanced Telecommunications Capability

Dear Ms. Dortch:

On October 8, 2002, Jim Smith, Don Cain, Gary Phillips, Christopher Heimann, Jim Lamoureux and the undersigned representing SBC Communications, Inc. (SBC), met with Michelle Carey, Rob Tanner, Claudia Pabo, Gina Spade, Daniel Shiman, Brent Olson, Ben Childers, and Jeremy Miller of the Competition Policy Division of the Wireline Competition Bureau and Jerry Stanshine, Jeff Goldberg and Shanti Gupta of the Network Telecommunications Division of the Office of Engineering and Technology.

The purpose of the meeting was to discuss the competitive deployment and usage of switches in the context of the Commission's Triennial Review. SBC also suggested a nine-month transition plan for moving the embedded base of UNE-P lines to UNE-L, resale or a business-to-business solution. The plan included an initial period to coordinate transition plans and intermediate intervals for CLECs to submit orders in order to minimize opportunities for parties to game the system. The attached material was discussed during the course of the meeting.

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Please contact the undersigned at (202) 326-8847 should you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to be 'K. J. R.' with a stylized flourish at the end.

Attachment

cc: Michelle Carey (w/o attachment)
Rob Tanner (w/o attachment)
Claudia Pabo (w/o attachment)
Daniel Shiman (w/o attachment)
Brent Olson (w/o attachment)
Ben Childers (w/o attachment)
Jeremy Miller (w/o attachment)
Jerry Stanshine (w/o attachment)
Gina Spade (w/o attachment)
Jeff Goldberg (w/o attachment)
Shanti Gupta (w/o attachment)



Unbundled Switching, UNE - P & Market Transition

October 8, 2002

Switching & UNE-P Overview



- Competitive switches are plentiful
 - Currently serving both residential and business customers
 - In large and small markets
- Intermodal competition is a reality
- UNE-P harms to telecom sector are widespread
 - Wireline carriers, manufacturers & intermodal competitors
- FCC should
 - Remove unbundled switching from the national UNE list
 - Preclude states from reinstating unbundled switching

Competitive Switches Are Widely Deployed & Used



- CLECs have deployed 1,300 circuit switches
(Fact Report, II-1 & Appendix B)
 - 200+ CLECs of all sizes have deployed local circuit switches in the BOC regions (Fact Report, II-1)
 - Including in small markets such as Apple Valley MN, Mishawaka, IN, Mojave CA, & Anniston AL (Fact Report, Appendix B)
- In addition to the circuit switches, more than 9,500 CLEC packet switches provide further competition (ALTS Local Competition Report 2002, page 16)

Competitive Switches Are Widely Deployed & Used



Percentage of Access Lines in Wire Centers Where CLECs Have Acquired Customers Through Ported Numbers		Percentage of BOC Switched Access Lines in Wire Centers Served by:									
		1 or more CLEC switch		2 or more		3 or more		4 or more			
		Bus.	Res.	Tot.	Bus.	Res.	Tot.	Bus.	Res.	Tot.	
VERIZON	90	83	85	84	75	79	80	69	73	75	68
SBC	88	83	85	82	75	77	74	66	69	70	65
BELLSOUTH	94	90	91	85	79	80	79	71	74	73	67
QWEST	89	83	85	82	75	77	75	68	71	71	66
TOTAL	89	84	86	83	76	78	77	68	71	72	66

CLEC switches reach customers representing 86% of BOC access lines. (Fact Report, II-6)

Competitive Switches Serve Residential and Business Customers



- Switches used to serve large business customers also serve mass-market customers (Fact Report, II-4)
- CLECs were serving about 3M residential lines, out of approximately 16-23 million total lines, using their own switches at EOY 2001 (Fact Report, II-4)

Growing Cable Telephony Competition



- Cable operators such as AT&T, Cablevision, Charter, RCN, Comcast and others provide telephony service to 2.2 million customers as of June, 2002
- Bill Schleyer of AT&T Broadband, “We finally have a national scale facilities based competitor to the ILEC. That is a very, very powerful position. . . . We’ll be taking a fair amount of share from [the ILECs] over the next few years.”
(AT&T Reply comments in AT&T/Comcast merger)
- AT&T’s own cable telephony operations “now have 115 franchise areas with greater than 25% penetration including dozens of communities within our largest markets.” (AT&T’s 2Q02 Investor Conference Call)
- Over the past 6 months cable has added 600,000 new telephony subscribers
 - that’s an average of 100,000 per month, a 40% increase from year end 2001

Growing Wireless Substitution



- As of February 2002, there were 130 million wireless subscribers. Up from 34 million at the end of 1995. (Fact Report, II-34)
- Two in five Americans have a mobile phone
(Fact Report, II-34)
 - Commission's Sixth CMRS Report issued July , 2001 found the wireless phone has become a mass market device and that 3 in 10 users prefer wireless phone to their landline phone (Fact Report, II-37)

Growing Wireless Substitution



- Yankee Group Report September 2002:
 - “Wireline networks... are the principal victims of mobile’s advance”
 - ~ 30% of personal calling minutes are now wireless
 - By 2006, the study predicts U.S. mobile subscribers will increase by 50% and will dominate personal calling, severely cannibalizing wireline minutes of use.
- The increasing trend toward the abandonment of landline connections seems to be a natural outgrowth of the advances in technology, lower pricing and more aggressive marketing by wireless companies.
(Eastern Management Group)
- “We expect continued weakness in access lines, as substitution to wireless, cable telephony and broadband remains an issue.”
(Morgan Stanley - July, 2002)

Claims that UNE-P is a Necessary Transitional Vehicle are Just a Smokescreen



- In NY, ATT and WCom operate 28 switches. Interestingly, they serve over one million residential customers with UNE-P, but have not converted a single residential customer to their switches.
- In SBC territory no significant conversions have occurred.
- It would be illogical to use it as anything other than a parking lot
 - ATT getting 45% return on no capital investment.
- Some UNE-P CLECs, such as Z-Tel, flat-out admit they have no plans to offer facilities-based service
- “[T]here is no empirical or theoretical basis for the argument that a new entrant must establish market share in advance of building facilities in order to have incentive to make investments necessary to enter a market.”

(Shelanski Reply Declaration, page 4)

CLEC Statements Confirm UNE-P Is Not A Transition Vehicle



“We’re profitable everywhere we sell because we limit ... where we sell based on cost.... [W]e’re deploying very little capital to make it work.”

Wayne Huyard, COO, MCI

“We do not expect that the growth of our business will require the levels of capital investment in fiber optics and switches that existed in historical telecommunications facilities-based models.”

Z-Tel 10-Q Filing

“Our principle of maximizing cash requires that we only enter states that meet our gross margin requirements.”

“We are not going into states where we don’t have a gross margin of 45% on the local”

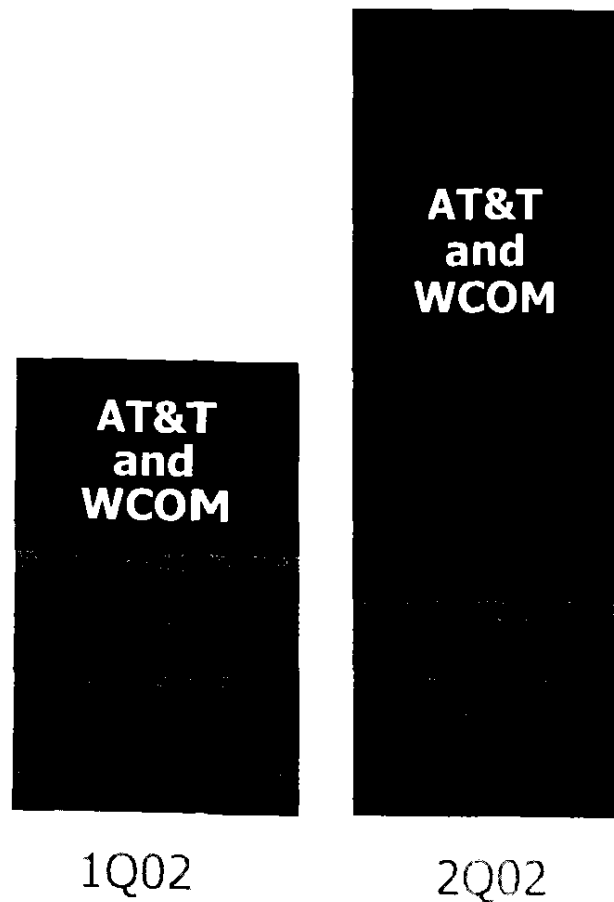
Betsy Bernard,

President, AT&T Consumer

UNE-P Predominantly Used by the Two Largest IXC's



**SBC UNE-P Lines
Added Per Quarter**

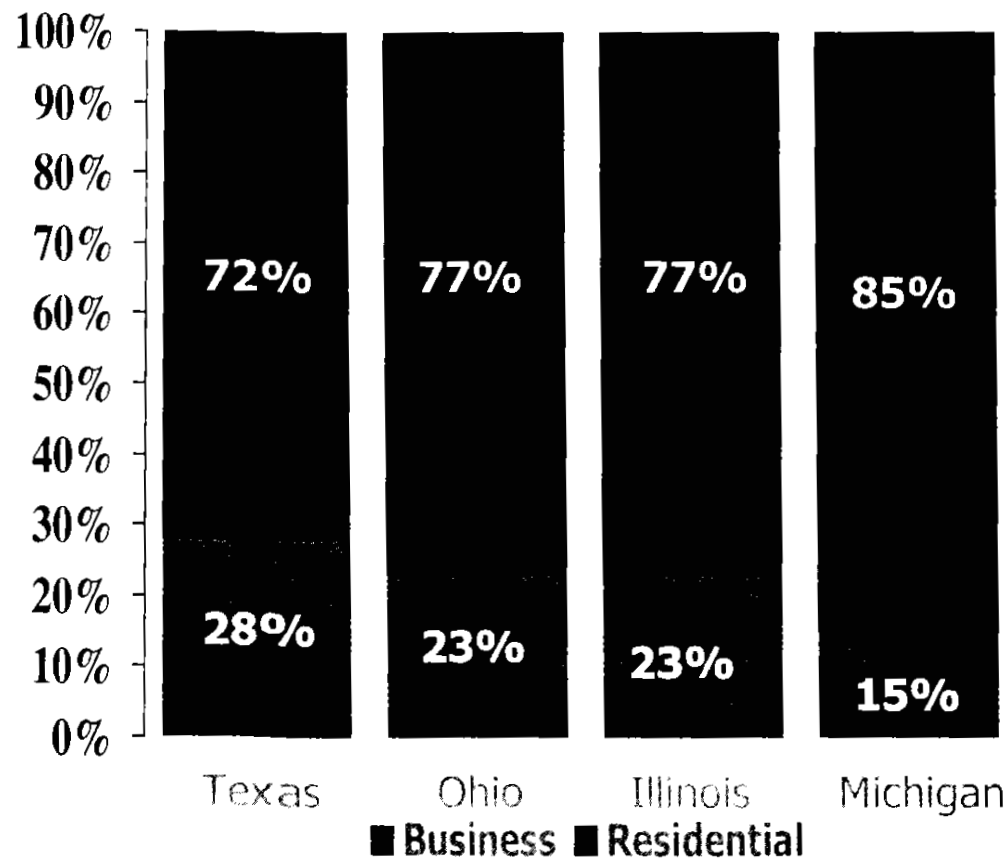


- More than 70% of SBC's UNE-P lines added in 2Q02 were for the two largest IXC's.
- From 1Q02 to 2Q02, UNE-P lines added for AT&T and WorldCom/MCI tripled while UNE-Ps added for others actually declined.

Residential Customers Are the Primary Target for UNE-P in SBC Territories



SBC UNE-P Lines In Service
SBC's Four Largest UNE-P States



- Across SBC's 13 states, more than 70% of all UNE-P lines are residential
- In SBC's four largest UNE-P states, which have been targeted most aggressively by the large IXC's, residential customers represent an even higher percentage of total UNE-Ps.

Negative Effects of UNE-P on Facilities-based Competition



➤ Credit Suisse First Boston recently “turned pessimistic about the extent to which Cox . . . will generate money from offering local telephone service over its cable TV systems” due to “the long distance carriers’ use of UNE-P [that] has picked up speed of late.” George Mannes, *Crowds Wiring Phone-Growth Hopes from Cox*, The Street.com (Sept. 19, 2002), <http://www.thestreet.com/tech/georgemannes/10043045.html> (citing Credit Suisse First Boston analyst Lara Warner).

➤ Legg Mason wrote: “the more successful the [Worldcom’s Neighborhood] plan is, the more it will reduce the attractiveness of the telephony opportunity for cable.”

Legg Mason, *WorldCom/MCI Bundled Phone Offer Challenges Rivals*, Regulators at 2 (Apr. 23, 2002).

Negative Effects of UNE-P on Facilities-based Competition



- “...current Federal telecom policy is fundamentally deflationary and unintentionally discourages investment and economic growth. The telecom/tech sector has gone from the propeller of the U.S. economy to an anchor to growth...”

(Precursor Group, October 2, 2001)

- “...Federal telecom policy: (1) creates regulatory dependence; (2) discourages investment and growth based on market forces; (3) devalues local access facility investment; (4) acts as a hidden multi-billion dollar regulatory tax on telecom investment; and (5) skews investment towards uneconomic data models.” (Precursor Group, October 2, 2001)

Telecom Manufacturers, Employment Harmed by Flawed Unbundling Rules



- Downbeat September 2002 vendor announcements
 - Alcatel announced that 3Q02 sales will fall 15% from 2Q02. The company will cut 20K more jobs over 18 months on top of 19,000 jobs cut in 2001
 - Lucent warned that 3Q02 sales could fall 25% from 2Q02. The company will announce “substantial additional layoffs” in 10/02, this is in addition to the 29,000 layoffs in fiscal 2001

Conclusions -



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- CLEC switches are serving customers virtually everywhere
 - Intermodal competition is a reality and competes head-to-head with wireline carriers
 - UNE-P undermines telecom investment impacting not only the carriers, but manufacturers as well
 - FCC should
 - Remove unbundled switching from the national UNE list
 - Preclude states from reinstating unbundled switching